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IN THE

Supreme Court of the United States

OCTOBER TERM, 1940.

No. 683.

THE UNITED STATES, *Petitioner,*

v.

HERBERT RIVINGTON PYNE, GRAFTON HOWLAND PYNE, MARY PYNE FILLEY, AND PERCY R. PYNE, JR., EXECUTORS OF THE ESTATE OF PERCY R. PYNE, *Respondents.*

On Petition for a Writ of Certiorari to the U. S. Court of Claims.

BRIEF FOR RESPONDENTS IN OPPOSITION TO THE PETITION.

ALLEN G. GARTNER,
Attorney for Respondents.
815 - 15th Street, N. W.,
Washington, D. C.

February, 1941.

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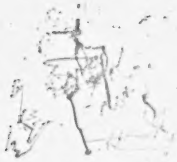

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On Petition for a Writ of Certiorari to the U. S. Court of Claims.

BRIEF FOR RESPONDENTS IN OPPOSITION TO THE PETITION.

The respondents herein oppose the petition for a writ of certiorari filed by petitioner, seeking a review by this Court of the judgment of the Court of Claims entered in the above-entitled cause on October 7, 1940.

OPINION BELOW.

The opinion and special findings of fact of the Court of Claims (R. 9-18) are reported in 35 F. Supp. 81.

JURISDICTION.

The judgment of the Court of Claims was entered October 7, 1940 (R. 19). The original judgment was entered for the amount of $16,542.80, with interest. A remittitur (R. 19) has been subsequently filed, reducing the amount of the judgment to $16,472.54, with interest. The jurisdiction of this Court has been invoked by the petitioner under Section 3(b) of the Act of February 13, 1925, as amended.

QUESTION PRESENTED.

Whether this Court will disturb the special findings of fact of the Court of Claims, finding that the decedent, prior to his death, and the executors of his estate thereafter, were engaged in business and therefore entitled to deduct from gross income of the estate, that part of the attorneys fees found to be attributable to the business operations of the estate with the further finding that the remaining part being attributable to the administration of the estate was not deductible.

STATUTE INVOLVED.

Revenue Act of 1934, c. 277, 48 Stat. 680:

"Sec. 162. *Net Income.* (U. S. C., Title 26, Sec. 162)
The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual,—

Sec. 23. *Deductions from Gross Income.* (U. S. C. Title 26, Sec. 23)
In computing gross income there shall be allowable as deductions:
(a) *Expenses.*—
(1) *In general.* All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, including a reasonable

allowance for salaries or other compensation (including the entire amount expended for meals and lodging) while away from home in the pursuit of a trade or business; and rentals or other payments required to be made as a condition to the continued use or possession, for purposes of the trade or business, of property to which the taxpayer has not taken or is not taking title or in which he has no equity."

STATEMENT.

The petitioner omitted many of the essential facts in its petition. There follows a full and corrected statement of the facts taken from the lower Court's special findings of fact.

Respondents are the executors under the will of Percy R. Pyne, who died August 22, 1929. They were authorized under the will to sell estate property, reinvest the proceeds, participate in reorganization of corporations in which decedent held an interest, collect the income, distribute it and corpus as provided in the will and perform other duties. After payment of specific bequests, the residue passed to trustees under the will for the benefit of named parties. Under this latter provision, trusts were set up in 1935 (R. 9) at which time the residue passed to the trustees, who were also the executors and whose duties were similar to those of the executors as outlined above (R. 10).

Prior to and at the time of his death, the decedent was engaged in business as a financier and investor, maintaining an office where he employed an office manager and an average of six clerks. After his death, substantially the same office set-up was maintained by the executors and is maintained at the present time by the trustees. The decedent's estate was valued at approximately $35,000,000 at his death in 1929 and included 129 different issues of stock, 118 different issues of bonds and certain real estate (R. 12).

The executors were the three sons and a daughter of the decedent, all of whom had had but little business experience. The decedent's death having occurred just prior to the economic depression, beginning in 1929, they employed an at-

torney to advise them in matters both legal and economic that arose in the business activities of the estate regarding Federal estate and state inheritance taxes, the acquisition and disposal of securities and various matters pertaining to companies in which the estate held investments (R. 12-13).

The Federal estate tax matters were determined and closed in 1931 (R. 10). However, some matters pertaining to the payment of these taxes arose in 1934, the year here involved, and it was necessary for the attorney to perform some service in securing extensions of time for the payment of these taxes and other matters relating thereto, though such srvices were of a relatively minor character, as compared with the attorney's other services in advising the executors with respect to the general operation of the business affairs of the estate. In general, the operations of the estate continued in substantially the same manner after the decedent's death as before that time (R. 13).

The executors did not have any contract with the attorney for his services, but he was paid from time to time as he needed the money and requested payment, and as it suited the convenience of the estate (R. 13) that kept its books and rendered its returns on the cash receipts and disbursements basis (R. 11). During the period from the time he was engaged in 1929 to and including 1935, he was paid a total in fees of $450,000. In the year 1934, here involved, he was paid $40,000. for legal services and $155.60 as reimbursement for expenses incurred (R. 13).

In the income tax returns filed by the executors for the estate for 1934, they claimed as a deduction, other expenses amounting to $75,470.20. This item included salaries to office employees, $15,909.96; office rent, $4,931.32; office expenses, $3,474.11; and attorney's fees and expenses, $40,155.60—the item here in controversy. In his audit of the return, the Commissioner of Internal Revenue allowed all of the expenses itemized above except the attorney's fees and expenses of $40,155.60, which he disallowed on the ground that such amount was not deductible as a business

expense, but was an administration expense of the estate, resulting in a tax deficiency of $15,309.20 (R. 11). The executors duly paid this tax and filed claim for its refund on the ground that the estate was engaged in business, therefore, the attorney's fees constituted an expense incurred in connection with the conduct of the business affairs of the estate. Alternatively, it was claimed that if, as contended by the taxing authorities, the expense was an administration expense of the estate, the sum would have been deductible from the value of the estate for estate tax purposes and that subject having been closed in 1931, the Government thereby become unjustly enriched by having collected an estate tax on the value of the estate without having allowed a deduction for the attorney's fees in question (R. 12).

The claim for refund was rejected and suit was duly filed in the Court of Claims, where, after hearing the evidence, that Court made a special finding of fact that the decedent at and prior to his death and his estate were engaged in business and that the amount paid for attorney's services "was paid principally for services in connection with the business operations of the estate" ($38,155.60) "and to a minor extent for services with respect to final disposition of estate taxes and similar matters, the reasonable value of the services of the latter character, based upon a comparison of the former with the latter on the basis of the total compensation paid, not being in excess of $2,000." (R. 12, 13).

Upon the special finding of fact made by the Court, it awarded judgment for the executors in the proper amount of tax claimed for refund that resulted from its special findings.

ARGUMENT.

The fundamental question at issue before the lower court was one of fact, namely, whether the decedent and the estate were engaged in business. Secondarily, the court had to determine from the nature of services rendered by the at-

torney, whether his fees were a business expense, attributable to the income-producing business operations of the estate, or an expense of administering the estate. Its answer to the fundamental question was affirmative and it answered the secondary question by apportioning the legal expenses between deductible income-producing business expense ($38,155.60) and non-deductible expense ($2,000.00) pertaining to administration of the estate, in its finding of facts (R. 12, 13) which, under Rule 41 of the Revised Rules of this Court is in the nature of a special verdict.[1]

In treating with cases involving deduction of expenses, courts, and the Board of Tax Appeals have been uniform in considering each case on its own particular facts. Cf. *Deputy* v. *Dupont,* 308 U. S. 488, 496; 84 L. Ed. 416, 423. While the issue as to the deduction of sums of money paid out by the taxpayers in the two cases relied on by the petitioner are similar in that both taxpayers claimed the deductions as business expenses, nevertheless, the facts in those cases vary widely from the facts in this case and the issue in each instance turned on the particular facts as found by the trial Board in those cases.

In *City Bank Farmers Trust Co.* (*Duke Trust*) v. *Commissioner,* 112 Fed. (2d) 457, affg., 39 B. T. A. 29, the taxpayer, as trustee, pursuant to a court decree entered in connection with an intermediate accounting, paid to itself and charged to corpus, the trustee commissions fixed and allowed by the court under a state statute for receiving principal and paying it out. It did not deduct this commission in the tax return filed, but later sought the allowance of the deduction in a proceeding before the Board of Tax Appeals involving other non-related issues. From the stipulated facts, the Board decided that the exercise of the

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[1] *Mahan* v. *U. S.,* 14 Wall 109, 111, 20 L. Ed. 764, 765; *U. S.* v. *Smith,* 94 U. S. 214, 24 L. Ed. 115; *Stone* v. *U. S.,* 164 U. S. 380, 383, 41 L. Ed 477, 478, 17 S. Ct. 71; *Collier* v. *U. S.,* 173 U. S. 79, 43 L. Ed. 621, 19 S. Ct. 330; *Crocker* v. *U. S.,* 240 U. S. 74, 60 L. Ed. 533, 36 S. Ct. 245; *Niles Bement Pond Co.* v. *U. S.,* 281 U. S. 358, 360, 74 L. Ed. 902, 903, 50 S. Ct. 251; *U. S.* v. *Esnault-Pelterie,* 303 U. S. 26, 29, 82 L. Ed. 625, 628.

limited powers granted the trustee did not constitute the operation of a business, therefore, the commission could not be deducted from income as a business expense, adding that its decision made it unnecessary to pass on the question whether the fact that the commission was charged to corpus of the trust *under the surrogate's order* prevented its classification as a business expense. The Second Circuit affirmed the Board.

In *White* v. *Commissioner* (C. C. A.-3) not yet officially reported, but published in 404 C. C. H., paragraph 9712, affg., 40 B. T. A. 664, the legal expenses constituting attorney's fees and other expense items of a judicial proceeding brought for the construction of the provisions of a testamentary trust and of the will establishing it, which were fixed and directed by the court to be paid by the trustees "out of the principal of the trust of the residuary estate," were sought to be deducted from income as a business expense, upon the contention that the trust was engaged in business. Upon trial of the issue before the Board, it was found and decided that the sum paid could not be deducted, regardless of whether the trust was carrying on a trade or business, on the ground that, even assuming that it was in business, the expense was not incurred and paid *"in the management and control of the trust estate,* but in a proceeding for a judicial determination of the rights of the various legatees under the will and of the beneficiaries of the trust." The Third Circuit affirmed the Board.

Upon the facts found by the trial Board in these two cases just described, which are relied upon by the petitioner, there is no conflict with the instant case, wherein the trial Court's special findings of fact clearly state that the decedent prior to and at his death, was engaged in business and that the respondents continued his business after his death, during the administration of his estate. The further special finding (R. 13) allocating the attorneys fees between those services pertaining to the business operations of the estate's business affairs ($38,155.60) and those pertaining to the administration of the estate ($2,000.00) is the result of the

Court's full consideration to the evidence before it, including the detailed testimony of the attorney who rendered the services, which were purely of an advisory nature and did not include any trial proceedings. Furthermore, these special findings are in harmony with the Bureau's action allowing the amounts paid in the same year for office rent, salaries of office employees and office expenses, to be deducted as business expenses.

In *Higgins* v. *Commissioner*, 111 Fed. (2d) 795, affg. 39 B. T. A. 1005, the trial Board allocated the total expense incurred between deductible and non-deductible business expense, based upon the evidence before it and its action was not disturbed nor was it criticized by the Third Circuit upon review of the trial Board's decision.

The conflict asserted by the petitioner appears to be one more of fact than law. In view of this Court's rule, preventing the evidence upon which the lower court based its finding of fact from coming before it, such special finding becomes conclusive upon this Court[2] and there being no question of law involved, it is submitted that the petition for a writ of certiorari should be denied.

Respectfully,

ALLEN G. GARTNER,
Attorney for Respondents.
815 - 15th Street, N. W.,
Washington, D. C.

February, 1941.

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[2] *Desmare* v. *U. S.*, 93 U. S. 505, 23 L. Ed. 959; *Talbert* v. *U. S.*, 155 U. S. 45, 39 L. Ed. 64; *Stone* v. *U. S.*, 164 U. S. 380, 41 L. Ed. 477; *Crocker* v. *U. S.*, 240 U. S. 74, 60 L. Ed. 533; *Jacob Reed's Sons* v. *U. S.*, 273 U. S. 200, 71 L. Ed. 608; *C. & P. Telephone Co.* v. *U. S.*, 281 U. S. 385, 74 L. Ed. 921.

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